

Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 NEA-10 IO-13 ISO-00 SP-02 USIA-06 AID-05

EB-07 NSC-05 CIEP-01 SS-15 STR-04 OMB-01 CEA-01

CIAE-00 COME-00 FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03

LAB-04 SIL-01 L-03 H-02 ITC-01 AGR-05 AGRE-00 /121 W

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R 271747Z SEP 76

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 5952

TREASURY DEPT WASHDC

INFO AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMEMBASSY DUBLIN

AMEMBASSY NEW DELHI

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY TOKYO

AMCONSUL BELFAST

AMCONSUL EDINBURGH

USMISSION EC BRUSSELS

USMISSION OECD PARIS

USDEL MTN GENEVA

AMEMBASSY MANILA

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DEPARTMENT PASS FRB

TREASURY FOR DONALD SYVRUD, OASIA

MANILA PASS US DELEGATION TO BANK/FUND MEETING

E.O. 11652: N/A

TAGS: EFIN,UK

SUBJECT: THE CHANCELLOR ON THE ECONOMY

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SUMMARY: IN A WIDE RANGING TELEVISED INTERVIEW THE CHAN-

CELLOR OF THE EXCHEQUER GAVE NO SIGN OF ABANDONING HMG'S YEAR-OLD ECONOMIC STRATEGY. HE VIRTUALLY RULED OUT BROAD IMPORT CONTROLS, REPEATED HIS INTENTION TO ADHERE TO A 12 PERCENT RATE OF GROWTH IN MONEY SUPPLY. AND MAINTAINED HIS VIEW THAT REAL GDP WOULD GROW BY 4.5 PERCENT BETWEEN JUNE 1976 AND JUNE 1977. AWARE BOTH OF THE CRITICISM IN STORE FOR THE GOVERNMENT'S ECONOMIC STRATEGY AT THIS WEEK'S LABOR PARTY CONFERENCE AND OF LIKELY ADVERSE FOREIGN EXCHANGE MARKET REACTION TO ANY POLICY CHANGE DESIGNED TO MEET THAT CRITICISM, THE CHANCELLOR UNDERLINED HMG'S COMMITMENT TO ITS CURRENT COURSE. END SUMMARY.

1. IN A SEPTEMBER 27 TELEVISED INTERVIEW PRIOR TO HIS DEPARTURE FOR THE FAR EAST AND MEETINGS CULMINATING WITH THE IMF/IBRD SESSIONS IN MANILA. THE CHANCELLOR OF THE EXCHEQUER OUTLINED HIS VIEWS ON A SERIES OF KEY ECONOMIC ISSUES CURRENTLY FACING HMG.

IMPORT CONTROLS

RESPONDING TO GROWING DEMANDS FOR GENERAL IMPORT CONTROLS AS A MEANS OF REDUCING UNEMPLOYMENT, MR. HEALEY EXPRESSED HIS BELIEF THAT AN IMPORT DEPOSIT SCHEME WOULD ACTUALLY REDUCE EMPLOYMENT. HE BELIEVED THAT SUCH A REDUCTION WOULD COME ABOUT AS MORE FIRMS' LIQUIDITY POSITIONS WERE ERODED THEREBY REDUCING INVESTMENT AND CONSEQUENTLY EMPLOYMENT. AN IMPORT DEPOSIT SCHEME, ACCORDING TO THE CHANCELLOR, HAD ITS PRINCIPAL IMPACT IN THE FINANCIAL ARENA WHERE THE CURRENT ACCOUNT AND LEVEL OF INTERNAL LIQUIDITY WOULD BE AFFECTED OVER THE SHORT RUN. HOWEVER, WHEN THE SCHEME ENDED THESE EFFECTS WOULD BE REVERSED. THE CHANCELLOR CONCLUDED THAT HE COULD SEE "ABSOLUTELY NO EMPLOYMENT ADVANTAGE" FROM EITHER GENERAL IMPORT CONTROLS OR AN IMPORT DEPOSIT SCHEME "SO LONG AS I CAN RUN THE ECONOMY AS FAST AS IT CAN RUN."

MONEY SUPPLY

THE CHANCELLOR REITERATED HIS PREVIOUS VIEWS THAT PRESENTLY PLANNED PUBLIC EXPENDITURE LEVELS WOULD PERMIT THE RATE OF GROWTH OF THE MONEY SUPPLY (PRESUMABLY M3) TO LIMITED OFFICIAL USE

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BE HELD TO 12 PERCENT. HE COMPARED THIS FIGURE TO US AND FRENCH TARGETS OF 11.5 AND 12.5 PERCENT RESPECTIVELY.

STERLING

THE CHANCELLOR SAID THAT THE RECENT FALL IN STERLING FROM \$1.78 TO \$1.70 HAD RESULTED FROM THE RAPID RATE OF GROWTH IN THE MONEY SUPPLY OVER THE PAST 2 MONTHS, TALK OF NATIONALIZING BANKS AND INSURANCE COMPANIES, AND

THE THREAT TO INCOMES POLICY PRESENTED BY THE SEAMEN'S UNION WAGE DEMANDS. HE ADDED THAT NO FURTHER DRAWINGS ON THE \$5.3 BILLION STANDBY CREDIT HAD BEEN MADE BEYOND THE \$1.1 BILLION USED IN JUNE. HOWEVER, HE SAID THAT IT MIGHT BE NECESSARY TO DRAW A LITTLEORE FROM THE STANDBY FACILITY. WITH REGARD TO THE POSSIBILITY OF BORROWING FROM THE IMF, MR. HEALEY INDICATED IF HE DECIDED TO GO TO THE FUND IT WOULD BE ON THE ASSUMPTION THAT THE UK COULD GET THE NECESSARY ASSISTANCE WITHOUT ANY CHANGES IN ITS FISCAL POLICY.

THE ECONOMY

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THE CHANCELLOR AGAIN SPOKE OF THE LIKELIHOOD THAT GDP WOULD GROW BY 4.5 PERCENT IN REAL TERMS THROUGH MID 1977. HE EXPRESSED HIS BELIEF THAT UNEMPLOYMENT WOULD PEAK DURING THE FOURTH QUARTER OF 1976 AND WOULD FALL "THROUGHOUT 1977." HE STRESSED THAT INCREASED INVESTMENT AND HIGHER PRODUCTIVITY WERE THE KEY TO REDUCING UNEMPLOYMENT.

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2. COMMENT

THE CHANCELLOR SHOWED NO SIGN OF DEVIATING FROM THE ECONOMIC STRATEGY WHICH HMG PUT IN PLACE OVER A YEAR AGO. WHILE THIS STRATEGY IS COMING UNDER INCREASING ATTACK FROM CRITICS IN THE LABOR AND TRADE UNION LEFT ON THE GROUNDS THAT NEITHER EMPLOYMENT, INVESTMENT NOR THE CURRENT ACCOUNT HAVE BEHAVED IN THE MANNER PREDICTED BY THE GOVERNMENT, HMG SEES LITTLE ALTERNATIVE TO PERSISTING UNTIL PROGRESS BECOMES MORE EVIDENT. THE 4.5 PERCENT GROWTH RATE FORECAST OVER THE NEXT YEAR IS THE CHANCELLOR'S WAY OF ASKING FOR MORE PATIENCE FROM DOMESTIC CRITICS.

AT THE SAME TIME IT WAS CLEAR THAT MR. HEALEY WAS DIRECTING MUCH OF HIS MESSAGE TO INTERNATIONAL FINANCIAL OPINION.

ARMSTRONG

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